

Message Text

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FM AMEMBASSY SEOUL

TO SECSTATE WASHDC 9976

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EO 11652: N/A

TAGS: ETRA, GATT, MTN, KS

SUBJ: IMPACT OF PRIOR IMPORT DEPOSITS

REF: (A) STATE 226228, (B) SEOUL 6069

SUMMARY: THE EMBASSY HAS STUDIED THE KOREAN IMPORT DEPOSIT SYSTEM IN ITS VARIOUS COMPLEXITIES AND CONCLUDES THERE IS NO MEANINGFUL EVIDENCE TO SUPPORT A CONTENTION THAT IT DISCRIMINATES AGAINST IMPORTS FROM THE UNITED STATES. PART OF THE PROBLEM APPEARS TO BE PSYCHOLOGICAL AND PART DUE TO A MISUNDERSTANDING AS TO THE TIMING OF THE RETURN OF THE DEPOSIT, I.E., AT SETTLEMENT OF L/C RATHER THAN AT ARRIVAL OF GOODS. END SUMMARY

1. AS REQUESTED BY REFTEL, WE HAVE CONDUCTED A DETAILED EXAMINATION OF KOREA'S PRIOR IMPORT DEPOSIT SYSTEM IN AN ATTEMPT TO IDENTIFY THE IMPACT ON U.S. TRADE. OUR MOST SIGNIFICANT FINDING IS THAT THE CONTENTION THAT THE DEPOSIT SYSTEM, WITHOUT AN AUTOMATIC RETENTION PERIOD, DISCRIMINATES AGAINST MORE DISTANT SUPPLIERS DOES NOT HOLD UP UNDER CLOSE ANALYSIS. THIS CABLE FOCUSES ON THAT ASPECT OF THE SYSTEM. THE FULL REPORT, WHICH INCLUDES A BROADER DISCUSSION ON HOW THE SYSTEM AFFECTS IMPORTS AND ADDRESSES OTHER POINTS IDENTIFIED

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IN THE REFTEL, IS BEING FORWARDED BY AIRGRAM.

2. IT HAS BEEN CONTENDED AT LEAST AS LONG AGO AS THE SECOND MINISTERIAL CONFERENCE THAT KOREA'S IMPORT DEPOSIT SYSTEM DISCRIMINATED AGAINST MORE DISTANT SUPPLIERS BECAUSE: (1) IT WAS ASSESSED ON THE BASIS OF C.I.F. VALUE, THEREBY MAGNIFYING THE DISADVANTAGE OF HIGHER FREIGHT COSTS; AND (2) DEPOSITS HAD TO BE MAINTAINED LONGER FOR IMPORTS FROM MORE DISTANT SOURCES. THE FIRST POINT WAS ELIMINATED WITH THE CHANGE IN 1974 TO ASSESSING THE DEPOSIT ON THE F.O.B. PRICE PLUS 10 PERCENT. OUR ANALYSIS NOW INDICATES THAT THE SECOND POINT NEVER HAD MUCH VALIDITY.

3. THE FLAWS IN THE PREVIOUS REASONING HAVE BEEN: (1) TO ASSUME THAT THE DIFFERENCE IN THE AVERAGE INTERVAL BETWEEN THE POSTING OF A DEPOSIT AND THE RELEASE OF THE DEPOSIT FOR IMPORTS FROM THE U.S. AS COMPARED TO IMPORTS FROM JAPAN IS GREATER THAN IT ACTUALLY IS; AND, MORE IMPORTANTLY, (2) TO ATTRIBUTE THAT DIFFERENCE LARGELY TO JAPAN'S GREATER PROXIMITY TO KOREA. THE LATTER ERROR HAS ARISEN FROM A TENDENCY TO ASSUME A CLOSE RELATIONSHIP BETWEEN ACTUAL ARRIVAL OF THE COMODITY AND THE RELEASE OF THE DEPOSIT. HOWEVER, IN THE ABSENCE OF A RETENTION PERIOD, DEPOSITS ARE RELEASED AT THE TIME OF "SETTLEMENT". SETTLEMENT, IN THIS SENSE, OCCURS WHEN THE SHIPPING DOCUMENTS ARRIVE IN KOREA. WHEREAS THERE IS A DIFFERENCE OF A MONTH OR SO IN SHIPPING TIME FROM THE U.S. AS COMPARED TO JAPAN, THE DIFFERENCE IN THE AVERAGE TRANSIT TIME FOR FORWARDING SHIPPING DOCUMENTS IS FOUR OR FIVE DAYS, AT MOST, AND PROBABLY LESS. (ACCORDING TO VARIOUS ESTIMATES OBTAINED FROM BANKING AND IMPORTING COMMUNITY SOURCES, SHIPPING DOCUMENTS FROM THE U.S. ARRIVE IN ABOUT A WEEK TO TEN DAYS FOLLOWING SHIPMENT AS COMPARED TO ABOUT FIVE DAYS FOR SHIPPING DOCUMENTS FROM JAPAN).

4. ALTHOUGH WE HAVE BEEN CONSCIOUS FOR SOME TIME OF THIS DISTINCTION BETWEEN SETTLEMENT AND THE ARRIVAL OF THE COMMODITY AS FAR AS THE DEPOSIT SYSTEM IS CON-
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CERNED, OUR CONTINUED ARGUMENT THAT THE AVERAGE INTERVAL BETWEEN OPENING OF THE L/C AND SETTLEMENT (HEREAFTER REFERRED TO AS THE L/C-SETTLEMENT INTERVAL) IS LONGER FOR IMPORTS FROM THE U.S. THAN FOR IMPORTS FROM JAPAN WAS NEVER CHALLENGED BY ROKG OFFICIALS WITH WHOM WE DISCUSSED THE ISSUE. THERE IS, IN FACT, A DIFFERENCE, ALTHOUGH IT IS SMALLER THAN WE HAD ASSUMED. A RECENT ROKG MINISTRY OF FINANCE (MOF) ANALYSIS INDICATES THE

AVERAGE L/C-SETTLEMENT INTERVAL IS ABOUT FOUR WEEKS FOR OVERALL IMPORTS FROM JAPAN; SIX WEEKS FOR OVERALL IMPORTS FROM THE U.S.; AND EIGHT WEEKS FOR OVERALL IMPORTS FROM EUROPE.

5. AS A RESULT OF OUR ANALYSIS, WE HAVE CONCLUDED THAT DIFFERENCES ARE LARGELY THE RESULT OF THE DIFFERENT MIX OF IMPORTS FROM THOSE THREE SOURCES AND HAVE LITTLE, IF ANYTHING, TO DO WITH DIFFERENCES IN PROXIMITY TO KOREA. FOR EXAMPLE, IN RESPONSE TO THE SPECIFIC QUESTION OF WHETHER THERE IS ANY SIGNIFICANT DIFFERENCE THE AVERAGE L/C-SETTLEMENT INTERVAL FOR AN IMPORT OF THE SAME TYPE OF COMMODITY FROM THE U.S. AS COMPARED TO JAPAN, WE FOUND VIRTUALLY UNANIMOUS AGREEMENT AMONG BANKING AND IMPORTING COMMUNITY SOURCES CONTACTED THAT ANY DIFFERENCE WAS MARGINAL AT MOST. THIS POINT IS DEVELOPED IN GREATER DETAIL IN OUR AIRGRAM. THE AIRGRAM ALSO DISCUSSES THE QUESTION OF WHETHER THE DEPOSIT SYSTEM TENDS TO AT LEAST WORK TO THE DISADVANTAGE OF OVERALL U.S. IMPORTS BECAUSE OF THE MIX OF THOSE IMPORTS AND CONCLUDES THAT IT DOES NOT.

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6. DESPITE ALL OF THE ABOVE, THERE MAY STILL BE SOME PROBLEM WITH HOW SOME IMPORTERS PERCEIVE THE IMPACT OF THE DEPOSIT SYSTEM ON IMPORTS FROM THE U.S. AS COMPARED TO IMPORTS FROM JAPAN. WHILE A MAJORITY OF THE IMPORTING COMMUNITY CONSIDERED THE DEPOSIT SYSTEM TO BE LARGELY

NEUTRAL IN THAT REGARD, WE ENCOUNTERED SEVERAL INSTANCES OF INDIVIDUALS WHO MAINTAINED THAT THE ELIMINATION OF THE RETENTION PERIOD WILL FAVOR JAPANESE IMPORTS. THE EXPLANATION, IN EACH INSTANCE, REVOLVED AROUND THE MECHANICS OF THE IMPORT SYSTEM AND IMPORTER PSYCHOLOGY. BECAUSE OF THE SHORT SHIPPING TIME FROM JAPAN, A COMMODITY IMPORTED FROM JAPAN TYPICALLY ARRIVES ALMOST SIMULTANEOUSLY WITH, AND FREQUENTLY A DAY OR TWO AHEAD OF, THE SHIPPING DOCUMENTS. THUS, THE IMPORTER CAN CLEAR HIS IMPORT THROUGH CUSTOMS IMMEDIATELY AFTER SETTLEMENT. IN THE ABSENCE OF A RETENTION PERIOD, THE IMPORT DEPOSIT IS ALSO RELEASED AT THIS TIME. IN PRACTICAL TERMS, ASSUMING THE IMPORTER IMMEDIATELY SELLS OR OTHERWISE DISPOSES OF THE IMPORT, HIS TRANSACTION IS COMPLETE AND HE HAS NO ADDITIONAL FINANCING COSTS. WITH A 90-DAY RETENTION PERIOD, IN CONTRAST, HE CONTINUES TO INCUR A FINANCING COST WELL BEYOND THE TIME OF SETTLEMENT. IN THE CASE OF THE TYPICAL IMPORT FROM THE U.S., THE IMPORTER MUST WAIT PERHAPS A MONTH OR SO BEYOND SETTLEMENT BEFORE THE COMMODITY ACTUALLY ARRIVES, IN TYING UP HIS MONEY WHILE HE WAITS FOR THE LIMITED OFFICIAL USE

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IMPORT, HE IS INCURRING A FINANCING COST BEYOND SETTLEMENT. WITH AN AUTOMATIC RETENTION PERIOD, HE TIES UP EVEN MORE MONEY, BUT THE ARGUMENT IS THAT THIS PROBLEM OF POST-SETTLEMENT FINANCING COSTS HAS ALWAYS EXISTED FOR IMPORTS FROM THE U.S., BUT HAS ONLY EXISTED FOR IMPORTS FROM JAPAN DURING THE OPERATION OF THE AUTOMATIC RETENTION PERIOD. GOING OVER THE ARGUMENT STEP-BY-STEP WE INVARIABLY CONCLUDED THAT THE PROPONENTS WERE CONFUSING THE NORMAL ADVANTAGE ACCRUING TO A NEARBY SUPPLIER WITH THE IMPACT OF THE DEPOSIT SYSTEM ITSELF. DESPITE OUR EFFORTS, THESE SOURCES CONTINUED TO INSIST THAT THE DROPPING OF THE RETENTION PERIOD FAVORED JAPAN. THESE SAME SOURCES, HOWEVER, QUITE READILY AGREED THAT THERE WAS LITTLE, IF ANY, DIFFERENCE IN THE AVERAGE L/C-SETTLEMENT INTERVAL FOR IMPORTING THE SAME TYPE COMMODITY FROM THE U.S. AS COMPARED TO JAPAN.

7. THE CIRCULATION OF THIS KIND OF ARGUMENT WITHIN THE TRADING COMMUNITY ITSELF MAY, IN FACT, EXPLAIN WHY PERIODIC COMPLAINTS ABOUT THE DISCRIMINATION OF THE IMPORT DEPOSIT SYSTEM AGAINST U.S. EXPORTS HAVE SURFACED OVER THE YEARS FROM SEEMINGLY KNOWLEDGABLE SOURCES. FOR THAT MATTER, A NORMALLY WELL-INFORMED MANAGER OF A U.S. BRANCH BANK STATED FLATLY TO AN EMBOFF THAT THE ELIMINATION OF THE RETENTION PERIOD WOULD CLEARLY DISCRIMINATE AGAINST U.S. IMPORTS. HE SUBSEQUENTLY RAISED THE ISSUE HIMSELF WITH FINANCE

MINISTER KIM YONG HWAN. KIM'S RESPONSE, AS REPORTED BY THE BANKER, WAS THAT HE WAS AWARE THAT DROPPING THE RETENTION PERIOD REINTRODUCED SOME DISCRIMINATION AGAINST MORE DISTANT SUPPLIERS, BUT HE FELT HONOR-BOUND TO RETURN TO THE OLD SYSTEM SINCE THE RETENTION PERIOD HAD BEEN PUBLICLY DESCRIBED AS A TEMPORARY MEASURE. KIM REPORTEDLY ADDED THAT MOF WOULD TRY TO FIND SOME OTHER MEANS OF BALACING OFF THIS ADVANTAGE FOR JAPANESE IMPORTS.

8. AS PART OF THIS LATEST STUDY, WE DISCOVERED THE ABOVE BANKER HAD BEEN UNDER THE IMPRESSION THAT THE DEPOSITS WERE RELEASED AT THE TIME OF THE ARRIVAL OF THE COMMODITY. AFTER VERIFYING WITH HIS BILLING LIMITED OFFICIAL USE

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DEPARTMENT THAT THE DEPOSITS, WITHOUT A RETENTION PERIOD, ARE RELEASED AT SETTLEMENT, HE CONCURRED IN OUR CONCLUSIONS. THE READINESS OF MINISTER KIM AND OTHER MOF OFFICIALS TO ACCEPT OUR PAST CONTENTIONS THAT THE DEPOSIT SYSTEM DISCRIMINATES AGAINST MORE DISTANT SUPPLIERS HAD APPARENTLY ARISEN FROM THE FACT THEY WERE CONSCIOUS THERE IS SOME DIFFERENCE IN THE AVERAGE L/C-SETTLEMENT INTERVAL FOR OVERALL IMPORTS AND THEY, LIKE WE, TENDED TO ASSUME THAT THE RELATIVE PROXIMITY OF JAPAN WAS AN IMPORTANT FACTOR IN THIS DIFFERENCE. MOF TECHNICIANS WHO WORK CLOSELY WITH THE DEPOSIT SYSTEM, HOWEVER, HAVE RIGHTLY BEEN SKEPTICAL OF THAT ASSERTION.
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